Processed Foods Outlook

U.S. Department of Commerce

International Trade Administration

Office of Consumer Goods

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July 2003

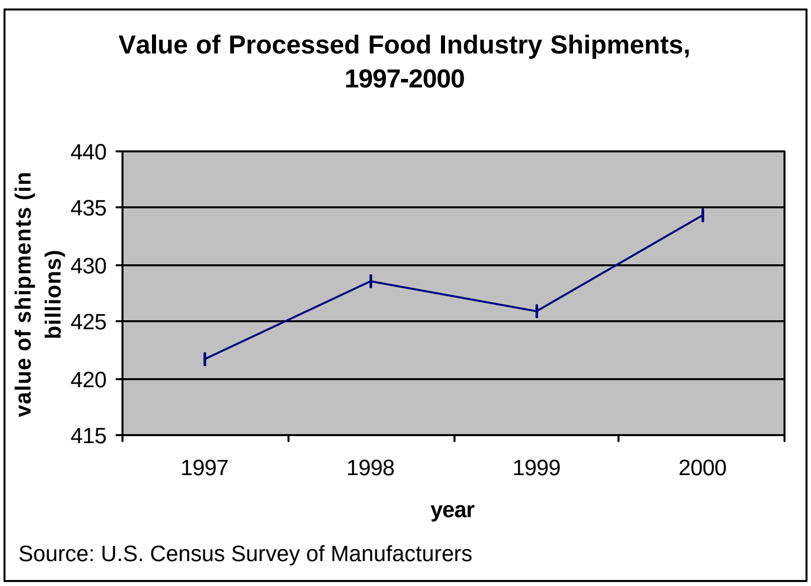
Food Manufacturing Industry Definition

The food manufacturing industry (NAICS 311) transforms livestock and agricultural products into products for intermediate or final consumption. Subsectors in this category include animal food manufacturing (NAICS 3111), grain and oilseed milling (NAICS 3112), sugar and confectionary product manufacturing (NAICS 3113), fruit and vegetable preserving and specialty food manufacturing (NAICS 3114), dairy product manufacturing (NAICS 3115), meat product manufacturing (NAICS 3116), seafood product preparation and packaging (NAICS 3117), bakeries and tortilla manufacturing (NAICS 3118), and other food manufacturing (NAICS 3119).

Establishments primarily engaged in manufacturing beverages and tobacco are classified separately in Subsector 312, Beverage and Tobacco Product Manufacturing and are not covered in this chapter.

U.S. Domestic Industry Overview

The food manufacturing industry is one of the United States' largest manufacturing sectors, accounting for about 10 percent of all manufacturing shipments. The processed food industry has seen slow but fairly steady growth over the last several years. In 2000, the value of food shipments was $434.3 billion, an increase of 3 percent from 1997 shipments of $421.7 billion (see chart).



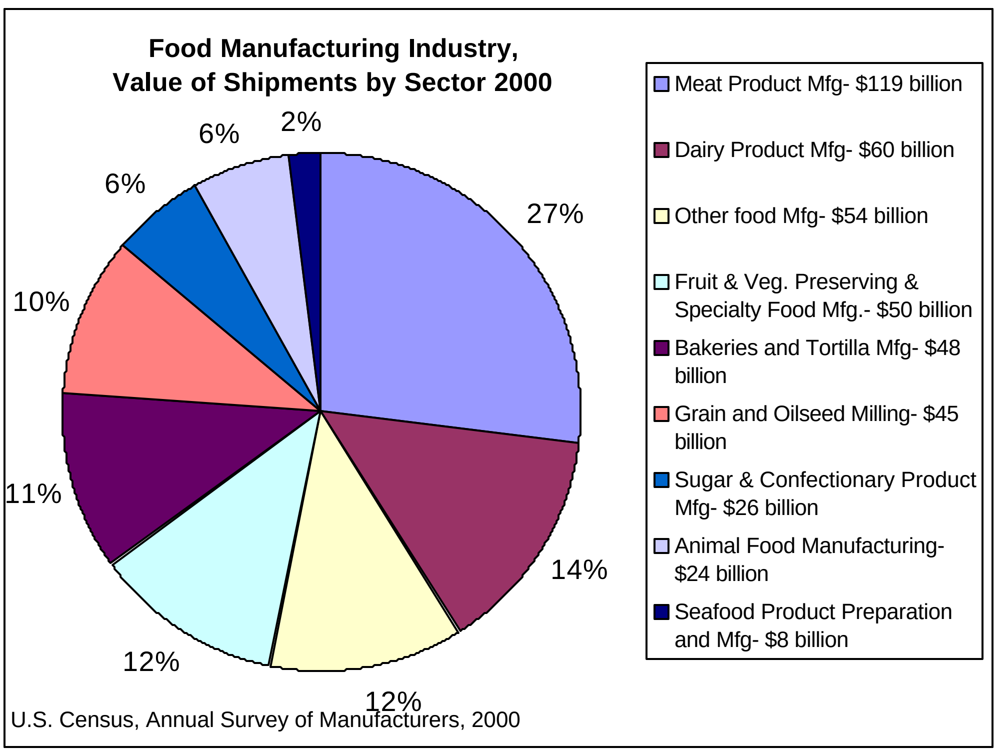
To remain competitive and increase profits, many companies in the industry have expanded production into foreign markets to take advantage of the needs of foreign consumers. The industry has also seen significant reorganization and consolidation in the last several years with many large companies merging to expand product lines, or consolidating plant facilities to contain costs. Technological change has also played an important role as the production process becomes increasingly automated and companies invest in new technology to increase productivity. Product innovation and increased spending on advertising are other areas where food manufacturers are trying to gain an edge.

Nature of the Industry

Processed foods are "value-added" products, referring to the fact that a raw commodity or commodities are transformed into a processed product through the use of materials, labor, and technology. Thus, any product that requires some degree of processing is referred to as a processed product, whether the processing level is relatively minor, such as for canned fruit or packaged cuts of meat, or more complex, such as for candy bars.

Many processed products are differentiated by well-known brand names, such as "Oreo" cookies or "Snickers" bars and are produced by multinational companies such as Kraft or Hershey. However, there are a number of processed products such as sugar that are not distinguished by national brand and are sold under generic or private label brands.

Of the subsectors that make up the food manufacturing industry, the largest four subsectors: meat products; dairy products; other food; and fruit and vegetable preserving and specialty food made up 65 percent of total industry shipment values of $434 billion in 2000. Other sectors included bakeries and tortilla manufacturing, which accounted for 11 percent, grain and oilseed milling (10 percent), animal food manufacturing (6 percent) and seafood products (2 percent).



Employment

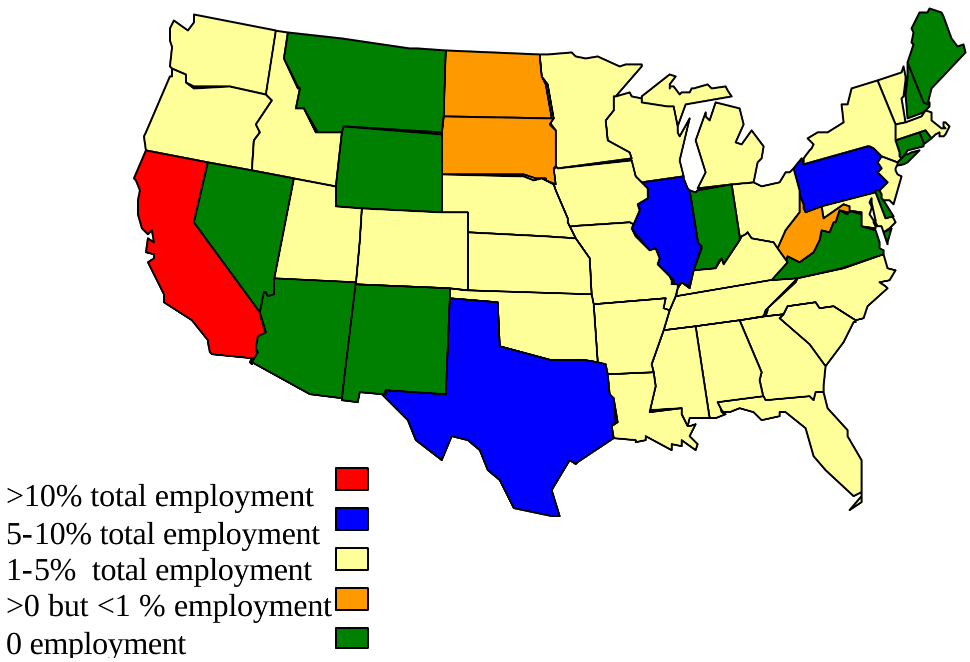
The food processing industry employed 13.2 million workers in 2002. The meat industry employed the largest percentage of workers in 2003 employing 40 percent of total workers in the industry. The preserved fruits and vegetables and bakery sectors each employed 16 percent and 15 percent of the industry respectively.

SIC Industry	Employment 2002 (thousands)	%
Food Products	1324.6	100.0
Meat products	522.6	39.5
Preserved fruits and veg.	213.5	16.1
Bakery Products	203.0	15.3
Dairy Products	145.9	11.0
Grain Mill Products	120.0	9.1
Sugar and Confectionary	91.5	6.9
Fats and Oils	28.1	2.1

Source: Bureau of Labor Statistics

Geographically, the largest percentage of workers in the industry is concentrated in California, making up 11 percent of the food processing industry workforce in 2002. Texas, Illinois, and Pennsylvania employed significant percentages of the food processing workforce at 7 percent, 6 percent, and 5 percent respectively with the rest of the workforce fairly evenly distributed across the United States (see chart).

2002 Employment in Processed Food Industry by State



Source: U.S. Department of Labor, Bureau of Labor Statistics, 2002 State Employment for Food Manufacturing

Increasing Consolidation

According to the Food Institute, the number of mergers and acquisitions by U.S. firms in the food manufacturing industry climbed to 240 in 1999 and then dropped to 171 in 2000. These numbers are significant, and reflect the fact that the industry continues to consolidate. The

Economic Research Service of the United State Department of Agriculture (USDA) notes that consolidation or mergers can be in a company's interest in order to take advantage of more efficient manufacturing plants and close inefficient ones, or quickly expand a firm's product lines by acquiring market share in a mature domestic market.

Consolidation among food retailers has also increased. As of 2000, the top four food retailers accounted for 27 percent of grocery sales, up from 16 percent in 1995. Although some believed that increased consolidation would lead to less competition and higher prices, this has not happened. Discount retailers such as Costco and Wal-Mart have stepped in to offer large volume food products at discounted prices. Also, more consumers are buying from restaurants and take out establishments, which compete with food retailers. According to USDA, spending on meals eaten away from home is accounting for a growing share of food spending and is expected to reach nearly 50 percent of total food expenditures by 2011. Competitive pressure between these three channels (warehouse clubs, traditional retailers, and restaurants) has kept the rise in food prices below inflation levels.

Food Prices

According USDA, the consumer price index (CPI) for food is projected to rise moderately from 2001 to 2011, increasing at an annual average rate of 2.1 percent. This is lower than the 2.5 percent average price rise expected in the CPI for all items and continues the long-term trend of food prices increasing at slightly less than the inflation rate. Due to sustained economic growth, consumer demand for food is expected to increase with rising disposable personal income. The strongest price increases for food consumed at home usually occur with the most highly processed foods such as cereals and bakery products. Because these prices depend more heavily on processing and marketing costs rather than farm commodity costs, they are more likely to rise at a rate closer to the general inflation rate. In 2001, 10 percent of household disposable personal income went towards food purchases.

Consumer Trends

Demographic and other factors are shaping demand for processed food products in the U.S. market. For example, as more women work outside the home and general consumers are short on time, convenience and snack foods are becoming more popular. Frozen foods are doing particularly well due to their convenient and quick preparation. Snack bars that are positioned as portable meals are in demand by consumers with little time for a sit down meal. Also, the Hispanic population in the United States is growing rapidly and processed food companies are targeting new products to this growing population.

Other factors changing the demand for processed food in the U.S. market are the concern and changing behavior about dieting and obesity, which are generating interest in weight-loss food products. The sports and fitness market is growing, and products that offer nutrition and energy benefits are popular.

Organic food is another market segment that is growing rapidly due to increased consumer interest in healthy products. Organic food can now be found in traditional supermarkets, natural food stores, and direct-to- consumer markets. The Organic Trade Association (OTA) said Americans spent $6.3 billion on organic food products last year, up from $1.6 billion five years ago. The trade group projects sales of $20 billion by 2005. USDA estimates that organic product sales will reach more than $11 billion in 2003 and will reach almost $22 billion in sales in 2010. Although USDA and OTA figures differ, both indicate the rapid growth of this segment of the processed food industry. Popular organic products include fresh produce, nondairy beverages, breads and grains, packaged foods, and dairy products. In response to rapid growth in the industry, USDA issued new Federal standards for organic food in October 2002. In accord with the new standards, a certified organic processed product must use at least 95 percent organic ingredients to be labeled or represented as organic.

Globalization and Impact on Processed Food Industry

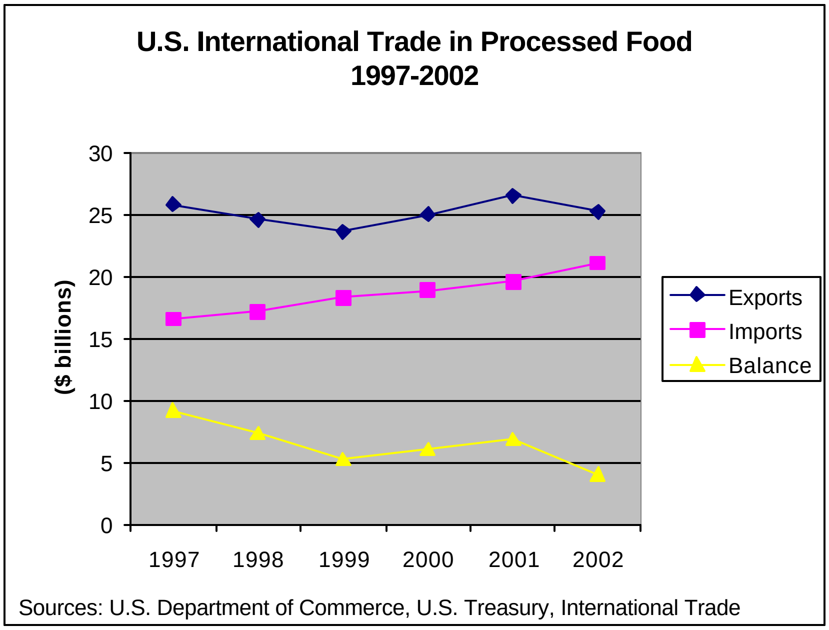
The U.S. processed food industry is a major participant in the global economy, active in both exporting and foreign direct investment. Almost half of the world's top 50 food processing firms are headquartered in the United States (21 out of 50 in 2003 according to Prepared Foods). Acquisitions and mergers have resulted in consolidation of some of the largest companies in the industry.

Global food consumption patterns are changing, leading to increased trade and demand for processed food products. Improvements in transportation, higher income, and consumer perceptions of quality and safety are important factors affecting sales of processed food. In developed countries, higher income growth has led to more demand for high value added and better quality processed food products. Income growth in developing countries has resulted in increased demand for meat products which may in turn drive demand for imports of products such as animal feed.

Standards for food safety vary across countries with wealthier countries often having stricter food safety regulations. Consumers in these countries are often willing to pay more for increased food safety. Differing standards for food safety can affect trade patterns since producers may find adhering to an exporting country's regulations costly. Alternatively, when domestic regulations are strict, domestic producers may face increased costs of production relative to importers and thus have an interest in applying the same sets of standards to their competitors. In response, countries are working within international organizations and multilateral trade agreements to move towards mutual recognition of systems and harmonization of standards.

U.S. Processed Food Trade

In 2002, the U.S. processed food industry exported more than it imported, $25.2 billion versus $21.1 billion. The trade balance narrowed slightly since 1997 from $9.2 billion to $4.1 billion.



Weakness in world economic growth in the first half of 2003 and the strength of the U.S. dollar slowed growth of U.S. processed food exports. As globalization and trade expand, the U.S. food processing sector becomes more heavily affected by conditions in world markets. Other factors that have a large impact on exports are rising incomes and their impact on dietary changes. In countries with low-income levels, consumers need basic calorie requirements and any increases in income lead to consumption of carbohydrates, which are high in calories. In higher income countries, consumers are able to meet their basic calorie needs and, thus, demand for food is driven by taste, cultural trends, quality, and convenience. Increased demand for these items can be met domestically and/or by increasing imports.

Top International Markets for Processed Food Products

In 2002, the largest share of U.S. processed food exports went to Canada, Japan, Mexico, Korea, and China (see chart). The U.S. imported the most processed food products from Canada, Mexico, Australia, New Zealand, and Italy.

The 1994 North American Free Trade Agreement (NAFTA) is one factor that spurred trade growth and foreign direct investment in processed food between Canada, the U.S., and Mexico. The United States is the largest source of foreign direct investment in Mexico's processed food industry. Because U.S. food processing affiliates in Mexico export only about 25 percent of their sales to the U.S., demand is dependent on the status of the Mexican economy. Increased trade and foreign direct investment between Mexico, Canada, and the United States, due to NAFTA, are creating a regional food market and can mean more efficiency in providing food to consumers due to extended growing seasons, expanded consumer choice, and increased food quality.

U.S. Trade Patterns in Food Manufacturing (NAICS 311) in 2002
(millions of dollars; percent)

Exports

Region	Value	Share, %
NAFTA	8,709	36
Latin America	2,148	9
Western Europe	2,745	11
Japan/Chinese Economic Area	5,874	24
Other Asia	3,172	13
Rest of World	1,456	6
Total	24,104	100

Top 5 Countries	Value	Share, %
Canada	5,120	21
Japan	3,838	16
Mexico	3,589	15
Korea	1,744	7
China	786	3

Imports

Region	Value	Share, %
NAFTA	8,116	41
Latin America	2,162	11
Western Europe	4,146	21
Japan/Chinese Economic Area	1,217	6
Other Asia	2,429	12
Rest of World	1,872	9
Total	19,942	100

Top 5 Countries	Value	Share, %
Canada	6,704	34
Mexico	1,412	7
Australia	1,290	6
New Zealand	1,017	5
Italy	923	5

Values may not sum to total due to rounding
Source: U.S. Department of Commerce, Bureau of the Census

According to the U.S. Department of Agriculture, the best markets for processed food exports in the top five countries were the following:

Canada: Snack foods, organic foods, seafood, pet food, processed meat

Japan: Pork, beef, tuna, crab, pet food, cheese, flatfish, prepared whole tomatoes, chocolate confectionary, fresh and frozen berries, frozen desserts, frozen pizzas

Mexico: Meat, fish and seafood, frozen desserts, sauces, snack foods, healthy foods, and food ingredients

Korea: Red meat, poultry meat, seafood, processed potatoes, frozen vegetables, sauces, confectionary, bakery products, pet food, processed fruits and vegetables

China: Red meat, poultry meat, dairy products, processed fruit and vegetables, snack foods, salmon, crab and crabmeat, tree nuts, fish paste, roe and urchin, egg products, pet food

Major Trade Shows for the Processed Food Industry

The following are major processed food trade shows supported by the U.S. Department of Agriculture. To search for future events, go to USDA's website at: http://www.fas.usda.gov/scripts/agexport/EventQuery.asp

- **U.S. Food Export Showcase & Food Marketing Institute's (FMI) Annual Exposition (Processed Foods)**

  May 2004
  Chicago, Illinois
  Number of visitors: 30000
  www.fmi.org/events/may

  USDA Contact: Sharon Cook
  USDA Trade Show Office
  1400 Independence Ave. SW
  Stop 1052
  Room 4939-South Building
  Washington, DC 20250
  Phone: 202-720-3425
  Fax: 202-690-4374
  Email: Sharon.Cook@usda.gov

- **World Food Moscow**

  September 23-26, 2003
  Moscow, Russia
  Number of visitors: 50000
  http://www.fas.usda.gov/agexport/shows/moscow2003.pdf

  USDA Contact: Ms. Tobitha Jones
  Room 4642-South Building
  14 Street & Independence Ave., SW
  Washington, D.C. 20250-1052
  Phone: 202-690-1182
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- **Foodex Japan 2004**

  March 2004
  Tokyo, Japan
  Number of visitors: 93637
  www.jma.or.jp/FOODEX/

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